

Message Text

PAGE 01 STATE 037666 TOSEC 040009

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ORIGIN SS-25

INFO OCT-01 ISO-00 SSO-00 CCO-00 /026 R

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TO USDEL SECRETARY AIRCRAFT IMMEDIATE

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C O N F I D E N T I A L STATE 037666 TOSEC 040009

EXDIS FOR ASST SECY ROGERS FROM RYAN

C O R R E C T E D C O P Y (CAPTION AND 1ST LINE OF TEXT
DROPPED AND SIGNATURE CHANGE)

E.O. 11652: GDS

TAGS: ENRG, OVIP, (KISSINGER, HENRY A.) VE

SUBJECT:IRANIAN HEAVY CRUDE PRICE OUT

SUMMARY: ANNOUNCEMENT BY IRAN OF PRICE CUT FOR HEAVY CRUDE
IS NOT EXPECTED TO HAVE DRAMATIC IMPACT ON SALES OF HEAVY
CRUDE OR ON COHESIVENESS OF OPEC. HOWEVER IT MAY PROVIDE
US OIL COMPANIES IN VENEZUELA WITH USEFUL AMMUNITION TO
PRESSURE GOV. END SUMMARY.

1. IRAN ANNOUNCED FEBRUARY 15 A CUT OF 9.5 CENTS PER
BARREL FOR HEAVY CRUDE THEREBY FOLLOWING ACTION TAKEN BY
KUWAIT LAST OCTOBER. VENEZUELA NOW ONLY MAJOR PRODUCER
OF HEAVY CRUDE HOLDING PRICE LINE.

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PAGE 02 STATE 037666 TOSEC 040009

2. OUR ANALYSIS INDICATES MAJOR PROBLEM IS CENTERED
AROUND WEAK DEMAND FOR HEAVY CRUDE IN INDUSTRIALIZED
NATIONS. THE PROLONGED ECONOMIC TURNDOWN COUPLED WITH
MILD WINTERS AND SOME SUBSTITUTION OF STEAM COAL AND NATURAL

GAS FOR HEAVY FUEL OIL HAS SIGNIFICANTLY CUT DEMAND. A SLOW AND MODERATE ECONOMIC RECOVERY CANNOT BE EXPECTED TO BOOST DEMAND SUBSTANTIALLY IN THE SHORT TERM.

3. WE NOTE THAT FOLLOWING OCTOBER PRICE CUT, KUWAIT BOOSTED PRODUCTION BY APPROXIMATELY 400 THOUSAND BPD BUT

PRODUCTION CAPACITY IS STILL UNDERUTILIZED BY AN ADDITIONAL 1.4 MILLION BPD. THE PRICE CUT DOES NOT THEREFORE SEEM TO HAVE BEEN A MAJOR DEMAND STIMULANT.

4. IRAN'S ACTION WILL BRING ITS HEAVY CRUDES MORE IN LINE WITH THOSE OF KUWAIT AND COULD, AT THE MARGIN, BOOST PRODUCTION SOMEWHAT. HOWEVER, MARKET DEMAND WILL STILL REMAIN WEAK AND IRAN MAY FIND ITS INCREASE (IF ANY) COMING OUT OF THE KUWAITI MARKET SHARE.

5. SHOULD VENEZUELA CHOOSE TO FOLLOW SUIT IN PRICE CUTTING, THE SITUATION MAY WELL REVERT TO THE STATUS QUO ANTE THE OCTOBER KUWAITI MOVE. IN ESSENCE, WE SEE ONE PRODUCER BENEFITTING FROM A UNILATERAL PRICE CUT, BUT NOT ALL, GIVEN MARKET CONDITIONS AND THE VERY LIMITED ABILITY OF CONSUMERS TO SUBSTITUTE HEAVY CRUDES FOR LIGHT.

6. NEVERTHELESS, EXXON, GULF, ET AL CAN BE EXPECTED TO SEIZE UPON THE IRANIAN ACTION AS A MEANS OF PRODDING THE GOV TO TAKE A NEW LOOK AT ITS OVER-ALL PRICE STRUCTURE.

7. COMMENT: THE OVER-ALL SERIOUSNESS OF THE PROLONGED MARKET DISCRIMINATION AGAINST HEAVY CRUDE IS OF CONCERN TO OPEC AND WAS TO HAVE BEEN DISCUSSED AT THEIR ABORTED DECEMBER MEETING. THUS FAR WE UNDERSTAND THAT THEY LOOK UPON THE PROBLEM AS ONE OF DIFFERENTIALS AND HAVE NOT FOCUSED ON THE OVER-ALL MARKET DEMAND STRUCTURE. WE DO NOT EXPECT THEM TO MEET BEFORE JUNE, AT WHICH TIME THEY CAN BE EXPECTED TO GO INTO THE PROBLEM IN GREAT CONFIDENTIAL

PAGE 03 STATE 037666 TOSEC 040009

DETAIL. IN THE INTERIM, EACH COUNTRY (IN EFFECT) ESTABLISHES ITS OWN DIFFERENTIALS FOR GRAVITY AND OTHER FACTORS AND MARKET RESISTANCE REVEALS THE LIMITS OF CONTROL THE CARTEL IS ABLE TO EXERT DOWNSTREAM. INGERSOLL

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